



## CREATE A SIMPLIFIED AVERAGE TAX

Filing taxes is unnecessarily complicated for most Americans. While higher income earners employ tax accountants to take advantage of every complicated provision in the tax code, most filers are left to fend for themselves. Developing a simplified tax filing system would reduce compliance burdens for most taxpayers while preserving the traditional filing process for those who prefer to utilize it.

### BACKGROUND

The Federal Government forces most Americans to hunt for tax deductions and credits if they wish to pay the correct amount of taxes owed. If a taxpayer misses filing a provision he or she is legally entitled to take, the taxpayer may end up overpaying. Incorrect credit and deduction claims may result in substantial fines and penalties.

The internal revenue code currently requires higher-income earners to calculate their tax liability through a simplified tax filing system called the alternative minimum tax (AMT) as well as their traditional filing.<sup>1</sup> The AMT compels filers to pay the higher of the two resulting tax bills.

Tax simplification shouldn't be exclusive to the wealthiest Americans — either through the AMT or the employment of accountants. According to the Internal Revenue Service (IRS), the adjusted gross income (AGI) floor for the top 20 percent of individual income taxpayers was \$50,464 in 2017.<sup>2</sup> In other words, developing a tax simplification option for taxpayers with AGIs less than \$50,464, would cover roughly 80 percent of taxpayers.

From 2001 to 2017, the average tax rate for the bottom 75 percent of AGIs was 5.88 percent.<sup>3</sup> The bottom 50 percent of AGIs pay an even lower average rate of 3.46 percent.<sup>4</sup> While the average tax rate appears much lower than the marginal rate brackets published by the IRS, it reflects the taxes Americans actually pay to the Federal Government when various income exclusions, deductions, and credits apply. Using these rates as a starting point for tax calculations could radically simplify taxes.

### POLICY SOLUTIONS

Legions of lobbyists currently protect the myriad complexities of the current tax code. Rather than tinkering with the existing code, Congress should pass a simplified average tax (SAT) which would operate parallel to the traditional income tax system, much like the AMT, to make tax filing easier for most Americans.

Under a SAT, filers with AGIs below a certain threshold set by Congress (such as the \$50,464 mentioned previously) could calculate their tax liability by applying an IRS-published average tax for their AGI quartile to their current tax year AGI. Taxpayers filing the SAT would exchange the below-the-line deductions and credits for a significantly lower tax rate.

Unlike the AMT, which requires taxpayers to calculate tax bills under both systems and pay the higher amount, the SAT would serve as an optional simplified alternative for most taxpayers that would save time and might result in a lower tax bill as well.

<sup>1</sup> Internal Revenue Service, *Topic No. 556 Alternative Minimum Tax* (Jan. 28, 2019), <https://www.irs.gov/taxtopics/tc556>.

<sup>2</sup> Internal Revenue Service, *SOI Tax Stats - Individual Statistical Tables by Tax Rate and Income Percentile*, <https://www.irs.gov/statistics/soi-tax-stats-individual-statistical-tables-by-tax-rate-and-income-percentile>, Table 1, All Individual Returns Excluding Dependents: Number of Returns, Shares of Adjusted Gross Income (AGI) and Total Income Tax, AGI Floor on Percentiles in Current and Constant Dollars, and Average Tax Rates, by Selected Expanded Descending Cumulative Percentiles of Returns Based on Income Size Using the Definition of AGI for Each Year, Tax Years 2001-2017, <https://www.irs.gov/pub/irs-soi/17in01etr.xls>.

<sup>3</sup> Internal Revenue Service, *SOI Tax Stats - Individual Statistical Tables by Tax Rate and Income Percentile*, <https://www.irs.gov/statistics/soi-tax-stats-individual-statistical-tables-by-tax-rate-and-income-percentile>, Table 2. All Individual Returns Excluding Dependents: Number of Returns, Shares of Adjusted Gross Income (AGI) and Total Income Tax, and Average Tax Rates, by Selected Ascending Cumulative Percentiles of Returns Based on Income Size Using the Definition of AGI for Each Year, Tax Years 2001-2017, Total income tax divided by adjusted gross income, <https://www.irs.gov/pub/irs-soi/17in02etr.xls>.

<sup>4</sup> *Id.*